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Message Text

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61
ACTION ABF-01

INFO OCT-01 EA-07 ISO-00 AID-05 IGA-02 SS-15 SP-02 H-02

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C O N F I D E N T I A L SEOUL 9113

E.O. 11652: GDS
TAGS: AFSP-AGAO, EAID, KS
SUBJECT: GAO QUESTIONS RE POSSIBLE CHANGES IN TERMS OF PAST,
PRESENT AND FUTURE PL 480 LOANS

REF: SEOUL 9112

1. THIS IS PART II OF MESSAGE REQUESTING APPROVAL OF DRAFT REPLIES TO GAO QUESTIONS ON PL 480 LOAN TERMS. PART I (REFTEL) TRANSMITTED GAO QUESTIONS AND PROPOSED GENERAL INTERIM REPLY. FOLLOWING IS DRAFT REPLY TO SPECIFIC GAO PROPOSALS CONTAINED IN THEIR QUESTIONS. OUR REPLY IS DRAFTED FROM VIEWPOINT OF KOREAN SITUATION AND MAY NEED SUPPLEMENTAL STATEMENTS OR COMMENTS RE GENERAL USG LENDING POLICIES.

2. SUGGESTED REPLY FIRST GAO QUESTION (STATED IN PARA 2 C REFTEL):

AS A GENERAL PRINCIPLE, WE DO NOT FAVOR RENEGOTIATION OF PAST CONTRACTUAL AGREEMENTS THAT DO NOT PROVIDE FOR RENEGOTIATION. ATTEMPTS BY ONE PARTY TO SECURE MORE FAVORABLE TERMS ON A RETROACTIVE BASIS UNDERMINE THE MEANING OF ALL AGREEMENTS AND INVITE ATTEMPTS BY THE OTHER PARTY TO CHANGE OTHER AGREEMENTS TO ITS ADVANTAGE. SUCH ATTEMPTS UNSETTLE THE WHOLE FABRIC OF BILATERAL AND INTERNATIONAL GOVERNMENTAL AND PRIVATE AGREEMENTS AND CONTRACTUAL OBLIGATIONS. IN THE CASE OF KOREA, THE TERMS OF $776 MILLION OF PL480 SALES (OF WHICH $358 MILLION HAVE BEEN CONCLUDED) WERE AGREED AS PART OF AN UNDERSTANDING REACHED IN OCTOBER, 1971 WHEREBY KOREA WOULD RESTRICT TEXTILE EXPORTS TO
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THE U.S. WE SSEE NO OVERRIDING SPECIAL REASONS TO SEEK TO HARDEN

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PREVIOUSLY AGREED PL480 LOAN TERMS TO KOREA. AS EXPLAINED IN THE BACKGROUND REPORT PROVIDED THE GAO TEAM AND IN ANSWER (BELOW) REGARDING FUTURE PL480 LOANS, KOREA'S ECONOMIC AND DEBT-SERVICE OUTLOOK DOES NOT NOW WARRANT ANY HARDENING OF TERMS. IN FACT, THE REVERSE IS INDICATED. WE ARE THEREFORE OPPOSED TO ANY CHANGES IN THE PROVISIONS OF PL480 LOAN AGREEMENTS ALREADY CONCLUDED.

3. REPLY TO SECOND QUESTION (PARA 3 REFTEL): IN OUR VIEW, FUTURE PL480 LOANS TO KOREA FALL INTO TWO CATEGORIES: (1) LOANS TOTALLING $276 REMAINING TO BE CONTRACTED WITHIN THE FRAMEWORK OF THE UNDERSTANDING REACHED IN CONNECTION WITH THE OCTOBER, 1971 TEXTILE AGREEMENT; AND (2) ANY PL480 LOANS THAT MAY BE MADE AFTER THE 1971 UNDERSTANDING HAS BEEN COMPLETELY FULFILLED. REGARDING THE FIRST CATEGORY, IT HAS BEEN OUR CONSISTENT INTENTION, PUBLICLY STATED, TO CARRY OUT OUR PL480 OBLIGATIONS UNDER THE TEXTILE UNDERSTANDING, INCLUDING AMOUNTS OF SALES, INITIAL PAYMENTS, CURRENCY USE PAYMENTS AND LOAN TERMS. WE THEREFORE OPPOSE ANY CHANGE IN THE AGREED PROVISIONS FOR THE REMAINING PL480 SALES OF $418 MILLION AND LOANS OF $276 MILLION, FOR THE SAME REASONS APPLYING TO LOANS ALREADY CONTRACTED.

4. WITH REGARD TO TERMS OF PL480 LOANS THAT MAY BE MADE AFTER FULFILLMENT OF THE TEXTILE UNDERSTANDING, THESE SHOULD OBVIOUSLY BE DETERMINED BY WORLDWIDE LENDING POLICY AND KOREA'S ECONOMIC SITUATION AND PROSPECTS AT THAT TIME (WHICH IS LIKELY TO BE IN FY 1978 OR FY 1979). AT PRESENT THE OUTLOOK IS FOR A DETERIORATION RATHER THAN AN IMPROVEMENT IN KOREA'S DEBT-SERVICE RATIO THROUGH 1980, DUE TO ITS LARGE BALANCE OF PAYMENTS DEFICIT AND INCREASED DEFENSE BURDEN. IT THUS SEEMS LIKELY THAT KOREA WILL CONTINUE TO NEED A MIXTURE OF SOFT AND HARD LOANS, AS RECENTLY CONCLUDED BY THE INTERNATIONAL CONSULTATIVE GROUP FOR KOREA. WHILE HARDER TERMS WOULD YIELD HIGHER REPYAMENTS FOR THE U.S., THEY MIGHT SO BURDEN KOREA AS TO OFFSET THE PURPOSE OF U.S. ASSISTANCE. IN ANY CASE, THE DECISION ON PL480 LENDING AMOUNTS AND TERMS SHOULD BE MADE AT THE APPROPRIATE FUTURE TIME, RATHER THAN PREJUDGED AT THIS TIME. WE THUS CANNOT AGREE THAT THE PRESENT ECONOMIC OUTLOOK FOR KOREA JUSTIFIES THE CONCLUSION THAT FUTURE PL480 LOANS SHOULD HAVE A SHORTER REPAYMENT PERIOD OR HIGHER INTEREST RATES THAN HAVE PREVAILED IN RECENT CONFIDENTIAL

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AGREEMENTS.

5. AS REGARDS THE QUESTION OF PROVIDING IN FUTURE LOANS (AFTER FULFILLMENT OF THE TEXTILE UNDERSTANDING) FOR RENEGOTIATION OF PAYMENT TERMS AT LEAST ONCE EVERY FIVE YEARS TO TAKE ACCOUNT OF CHANGING ECONOMIC CONDITIONS, THIS IS AN APPEALING THEORETICAL PROPOSAL WHICH RAISES THE VERY HARD PROBLEM OF HOW THE DIFFERENT OBJECTIVES OF LENDER AND BORROWER CAN BE SETTLED BY NEGOTIATION

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ALONE, PARTICULARLY GIVEN THE ECONOMIC UNCERTAINTIES WHICH ALWAYS LIE AHEAD AND WHICH RESULT IN DIFFERENT ECONOMIC FORECASTS EVEN BY PERSONS HAVING THE SAME OBJECTIVE OR PERSPECTIVE. ONE DANGER IN SUCH AN APPROACH IS THAT OTHER BILATERAL MATTERS WOULD BE INTRODUCED INTO SUCH NEGOTIATIONS AS A MEANS OF SETTLING NATURAL DIFFERENCES, THUS FURTHER COMPLICATING INTERNATIONAL RELATIONS. WHILE IT MIGHT BE POSSIBLE TO AGREE WITH A BORROWER ON SOME OBJECTIVE CRITERION THAT WOULD OVER A CERTAIN PERIOD DETERMINE AN AGREED CHANGE IN TERMS, SUCH CRITERIA WOULD DIFFER IN DEFINITION AND AMOUNT FROM COUNTRY TO COUNTRY AND FROM TIME TO TIME DURING THE LIFE OF A LOAN. ALL OF THESE CONSIDERATIONS SEEM TO US TO ARGUE AGAINST A GENERAL PERIODIC RENEGOTIATION PROVISION BEING INSERTED IN ALL NEW LOAN AGREEMENTS. END OD DRAFT REPLY TO TWO QUESTIONS.
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